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INTERNATIONAL INVESTMENT RULE-SETTING: TRENDS, EMERGING ISSUES AND IMPLICATIONS

Note prepared by the UNCTAD secretariat[1]

Executive summary

This note highlights recent trends in international investment agreements and focuses on the evolution of bilateral investment treaties – the backbone of the international investment rules system. On the basis of an analysis of major trends in BIT evolution, the note then identifies implications and systemic challenges with regard to the future development of the international system of investment rules, in particular for developing countries.

[1] This document was submitted on the above-mentioned date as a result of processing delays.

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INTRODUCTION

1. In the absence of a global investment treaty, most international legal disciplines on the relationship between host countries and international investors have been developed at a bilateral level. Treaties establishing minimum guarantees regarding the treatment of foreign investment have existed for more than two centuries.[2] In the latter half of the 20th century, bilateral investment treaties (BITs) emerged as the first international agreements exclusively focusing on the treatment of foreign investment. In view of their similar legal structure, as well as the fact that the number of BITs has greatly increased, these agreements rank among the most important pillars in international law on foreign investment.

2. Bilateral treaties on the promotion and protection of investments of investors of one contracting party on the territory of the other contracting party date back to 1959, when the first BIT was signed between the Federal Republic of Germany and Pakistan. Since that time, BITs featured a relatively uniform content that had not changed markedly, apart from the introduction of provisions on national treatment and investor–State dispute resolution in the 1960s. Since the mid-1990s, however, the inclusion of investment protection provisions in other international investment agreements (IIAs), in particular free trade agreements, and the submission of a growing number of investment disputes to arbitration under investor–State dispute settlement provisions, have caused some innovations in BIT practice, resulting in greater variation among these agreements than in the past.

3. The following discussion highlights recent trends in IIAs. It then focuses on the evolution of BITs – the backbone of the international investment rules system. On the basis of an analysis of major trends in their evolution, the issues note identifies implications and systemic challenges with regard to the future development of the international investment rules system, in particular for developing countries.

I. RECENT TRENDS IN INTERNATIONAL INVESTMENT AGREEMENTS

4. The trend from previous years towards an expansion and increasing sophistication of international investment rulemaking at the bilateral, regional and interregional level continued in 2005 and 2006 (for the first half of which data are available). The evolving system of international investment rules contributes further to the enabling framework for foreign direct investment (FDI). At the same time, given the increasingly complex multilayered and multifaceted universe of IIAs, it is becoming more and more difficult to ensure that they remain coherent and function effectively.

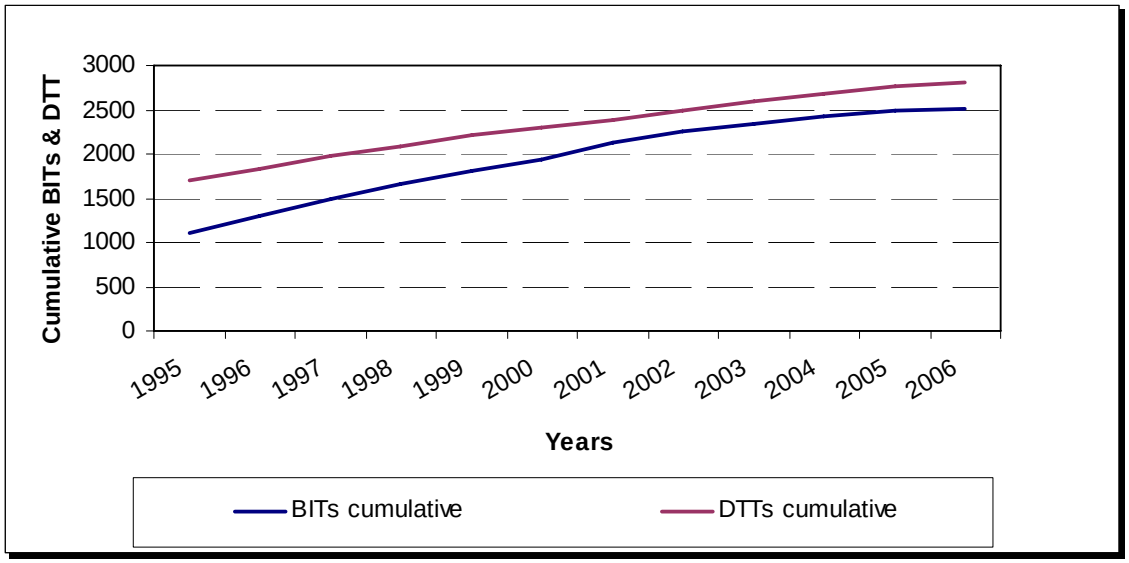
A. Bilateral investment treaties

5. Seventy new bilateral investment treaties (BITs) were concluded in 2005 and another 11 in the first six months of 2006, bringing the total number of BITs to a new peak of 2,506 at the end of June 2006 (figure 1). At the same time, the slowdown in the number of BITs concluded annually continued for the fourth consecutive year in 2005, and appears to have become more pronounced in 2006.

[2] The first Friendship, Commerce and Navigation Treaty signed between the United States and France in 1788 contained provisions regulating treatment of foreign investment.

6. More than half of the new BITs concluded involved developed countries: Belgium-Luxembourg and Finland were the most active for the second consecutive year, with nine and five new BITs respectively. Germany and Spain concluded four new agreements each.

Figure 1. Number of BITs and DTTs concluded, cumulative, 1995–June 2006

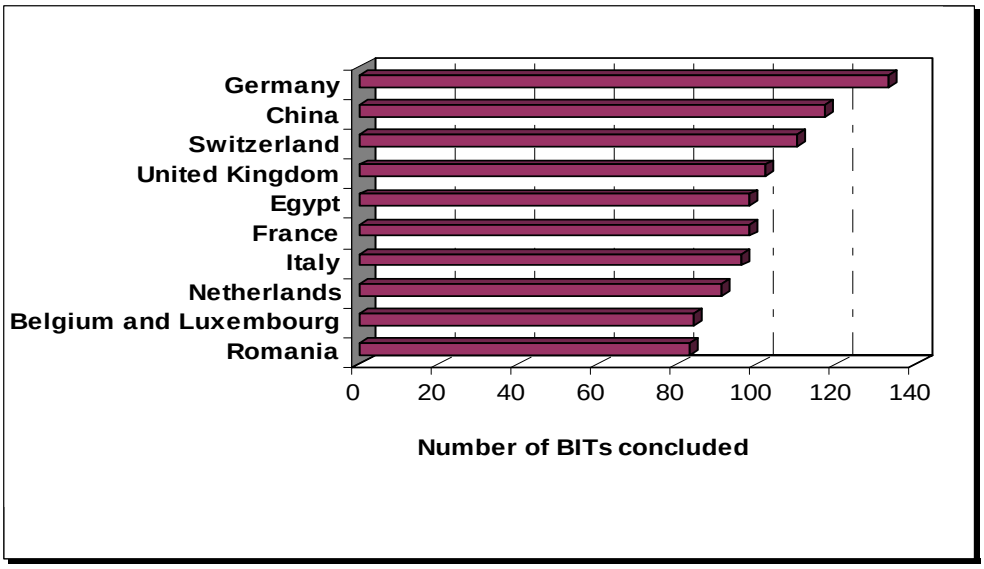


Source: UNCTAD (www.unctad.org/iia).

7. The participation of developing countries in the network of BITs continued to increase, as they were involved in 71 of the 81 new agreements. The number of South–South BITs has, however, declined from 28 agreements concluded in 2004 alone to 24 agreements between January 2005 and June 2006.

8. The trend towards the renegotiation of existing treaties also continued, with at least 14 BITs affected between January 2005 and June 2006. These include six agreements renegotiated by China with Belgium-Luxembourg, the Czech Republic, Portugal, the Russian Federation, Slovakia and Spain. Germany renegotiated BITs with Egypt and Yemen. China's strong involvement confirmed its position as the second country worldwide in terms of the number of BITs concluded. Belgium-Luxembourg was among the top ten BIT signatories for the first time (figure 2).

Figure 2. Top ten economies signatories of BITs, as of June 2006



Source: UNCTAD (www.unctad.org/iia).

9. As far as geographical coverage is concerned, European countries (excluding South-East Europe and the Commonwealth of Independent States (SEE&CIS)) concluded the highest number of BITs, with 49 new agreements between January 2005 and June 2006.

10. During the same period, African countries concluded 24 BITs, bringing the cumulative number of BITs for the region to 663 as of the end of June 2006 (table 1). Most active among African countries was Tunisia, with three new agreements, followed by Congo, the Democratic Republic of the Congo, Egypt and Sudan, with two new BITs each.

11. Asian countries concluded 35 BITs between January 2005 and June 2006. This brought the total number of BITs concluded by Asia and Oceania countries to 1,007 as of the end of June 2006 (table 1). Afghanistan concluded its second BIT in 2005 (with Germany), while China was the most active in the region, with 11 new BITs. Thailand and the Republic of Korea concluded four new BITs each.

12. Latin American and Caribbean countries were also active during these 18 months, with 15 new BITs concluded. Mexico was the most active country in the region, with four new BITs concluded with Australia, Iceland, Panama and Spain. Uruguay signed an amended BIT with the United States, replacing the 2004 agreement that was the first agreement which the United States had negotiated on the basis of its new model BIT. The number of Latin American and Caribbean BITs totalled 466 by the end of June 2006 (table 1).

13. The SEE&CIS countries signed 18 BITs between January 2005 and June 2006. The former Serbia and Montenegro set the pace in the region by concluding five new agreements with Cyprus, the Libyan Arab Jamahiriya, Switzerland, Egypt and Lithuania. This brought the total number of BITs concluded by SEE&CIS to 674 (table 1).

Table 1. International investment agreements concluded by regions 2005 – June 2006, and cumulative

Region	BITs		DTTs		Other IIAs	
	2005–June 2006	*Cumulative*	*2005–June 2006*	*Cumulative*	*2005–June 2006*	*Cumulative*
Asia and Oceania	35	1 007	53	985	18	95
Latin America and Caribbean	15	466	13	326	10	67
Africa	24	663	25	444	4	36
SEE&CIS	18	674	39	588	0	34
Memorandum						
Developed countries	50	1 516	45	2 118	16	136
Developing countries	71	1 889	78	1 629	26	197
South–South	24	648	35	409	9	89
Least developed countries	18	401	5	184	3	36[a]

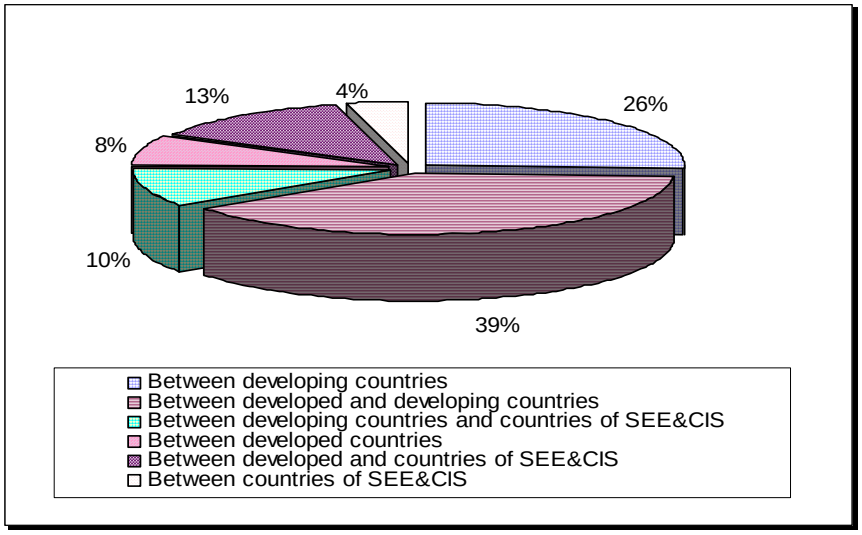
Source: UNCTAD

Note: The above figures reflect multiple counting (e.g. BITs concluded between countries from Asia and Africa are included in the list of *both* regions). The net total of each category of IIAs is therefore lower than the sum of the above figures.

[a] This number includes agreements concluded by regional groups that have one or more LDC members.

14. In terms of country groups, the largest number of BITs continues to be concluded between developed and developing countries. While earlier agreements almost exclusively fell into this category, a growing number of BITs now involve two developing countries (figure 3). In the last five years, the share of such agreements almost doubled (from 14 per cent to 26 per cent).

Figure 3. Total BITs concluded, as of end-June 2006, by country group



Source: UNCTAD (www.unctad.org/iia)

B. Double taxation treaties

15. In 2005, 78 new DTTs were concluded, and in the first six months of 2006, 41 were added, bringing the total number of DTTs to 2,799 by June 2006 (figure 1). During this 18-month period, Turkey was the most active country, concluding eight new DTTs, followed by Morocco and Spain, with seven new agreements each.

16. In terms of regional coverage, African countries concluded 25 new DTTs between January 2005 and June 2006, bringing the total number of DTTs concluded by this region to 444 (table 1). In addition to Morocco, South Africa, Egypt and Seychelles were among the most active in terms of the number of DTTs concluded.

17. Asian countries were particularly active during this period, concluding 53 new DTTs. This brought the cumulative number for Asia to 985 by the end of June 2006. Turkey ranked first in the region with eight DTTs, followed by India and Pakistan, with five new DTTs each.

18. Latin American and Caribbean countries concluded 13 new DTTs between January 2005 and June 2006, bringing the total number to 326 DTTs by the end of June 2006. Chile was most active in this region for the second consecutive year, with three new DTTs.

19. SEE&CIS countries concluded 39 DTTs between January 2005 and July 2006, bringing the total number of DTTs concluded by this region to 588. Croatia was the most active, concluding five new agreements, while Azerbaijan and Serbia and Montenegro concluded four new DTTs each.

20. About 31 per cent of all DTTs that were concluded in 2005 and the first six months of 2006 were between developing countries, while 21 per cent were concluded between developed and developing countries. This represents an important development, since in the past DTTs have predominantly been concluded between developed and developing countries. DTTs among developed countries accounted for 11 per cent only (down from 29 per cent at the end of 2004).

21. The regional distribution of all DTTs concluded by the end of June 2006 (by country group) remained more or less unchanged compared with 2004 (figure 4). Almost 40 per cent of all DTTs have been concluded between developing and developed countries. However, the share of DTTs between developed countries is significantly higher than in the case of BITs, which may be explained by the fact that double taxation poses a greater threat in these countries than political risk.

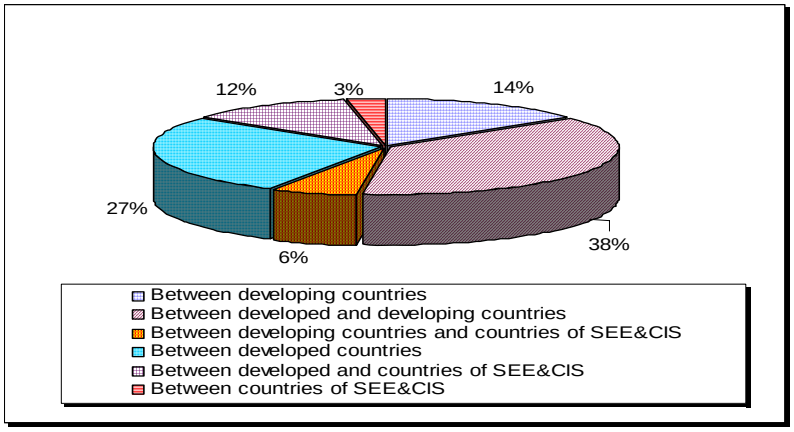
C. Preferential trade and investment agreements (PTIAs)

22. The tendency in previous years to establish international investment rules as part of preferential trade and investment agreements continued in 2005 and in the first half of 2006, albeit at a slower pace than in 2004.[3] The increase in PTIAs partly reflects a political will of a growing number of countries for closer economic cooperation. They may therefore prefer a comprehensive treaty covering trade and investment (and potentially also other areas) simultaneously. From the perspective of investment promotion, potential host countries might

3 These agreements appear under a variety of names, for example free trade agreements (FTAs), closer economic partnership agreements (EPAs), regional economic integration agreements or framework agreements on economic cooperation. For a detailed analysis, see UNCTAD (2006a).

also see the protection provisions within a broader legal framework as a way to increase their attractiveness to potential investors.

Figure 4. Total DTTs concluded, as of end-June 2006, by country group



Source: UNCTAD.

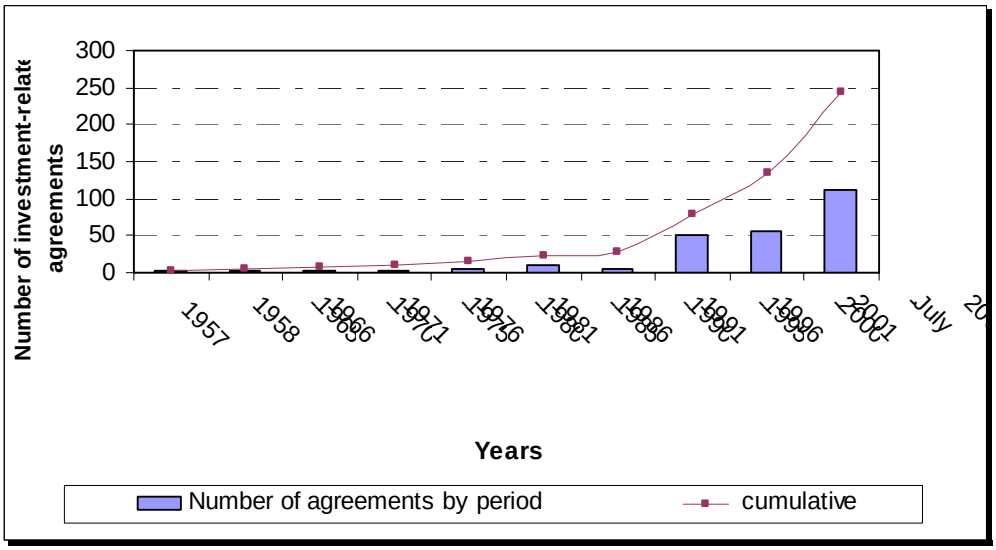
23. In addition to trade and investment, PTIAs may cover services, intellectual property, competition, labour, environment, government procurement, temporary entry for businesspersons and transparency, among others. This broad coverage demonstrates a trend towards an integrated approach when dealing with interrelated issues in international investment rulemaking (UNCTAD, 2006a).

24. Between January 2005 and July 2006, 26 new PTIAs involving 39 countries were concluded, bringing the total number of investment-related agreements to 244 as of the end of June 2006 (figure 5). Among the developing regions, Asian countries were the most active, with 38 per cent of the total PTIAs concluded by the end of June 2006, followed by Latin America, with 26 per cent, and by Africa and SEE&CIS countries, with 14 per cent each. Altogether, developing countries were parties to 79 per cent of the PTIA network, while developed countries were involved in 54 per cent of the agreements. South–South PTIAs also increased, reaching 89 agreements at the end of June 2006 (table 1).

25. While the total number of PTIAs is still small compared with the number of BITs (less than 10 per cent), it has nearly doubled over the past five years. In addition, as of 1 July 2006, at least 68 agreements involving 106 countries were under negotiation. This suggests an even more pronounced increase in such treaties in the near future.

26. Among the most important PTIAs concluded in 2005 and early 2006 were the Free Trade Agreement between the Republic of Korea and Singapore, the Economic Partnership Agreement between Japan and Malaysia, the Comprehensive Economic Cooperation Agreement between India and Singapore and the Free Trade Agreements between the United States and Oman, Peru and Colombia. These treaties establish, inter alia, binding obligations for the contracting parties concerning the admission and protection of foreign investment. The scope of the protection commitments is comparable to that found in BITs, including with regard to dispute settlement.

Figure 5. The growth of PTIAs, 1957 – July 2006
(Number)



Source: UNCTAD.

27. Other PTIAs that were signed in 2005 and the first half of 2006 only establish a framework for cooperation between the contracting parties. One example is the Framework Agreement on Comprehensive Economic Cooperation between ASEAN and the Republic of Korea. It provides for specific forms and areas of cooperation to promote investment, sets up an institutional framework to follow up on investment issues and establishes time frames for the launching of future negotiations on investment liberalization and/or protection. Other examples include the Trade and Investment Framework Agreement between the United States and Cambodia, which establishes an institutional framework in the form of a Council to identify investment opportunities and considers the need to conclude more substantive trade and investment agreements in the future.

28. These various treaty types offer countries a wide range of options for promoting and protecting international investment flows and for reflecting their specific level of economic development.

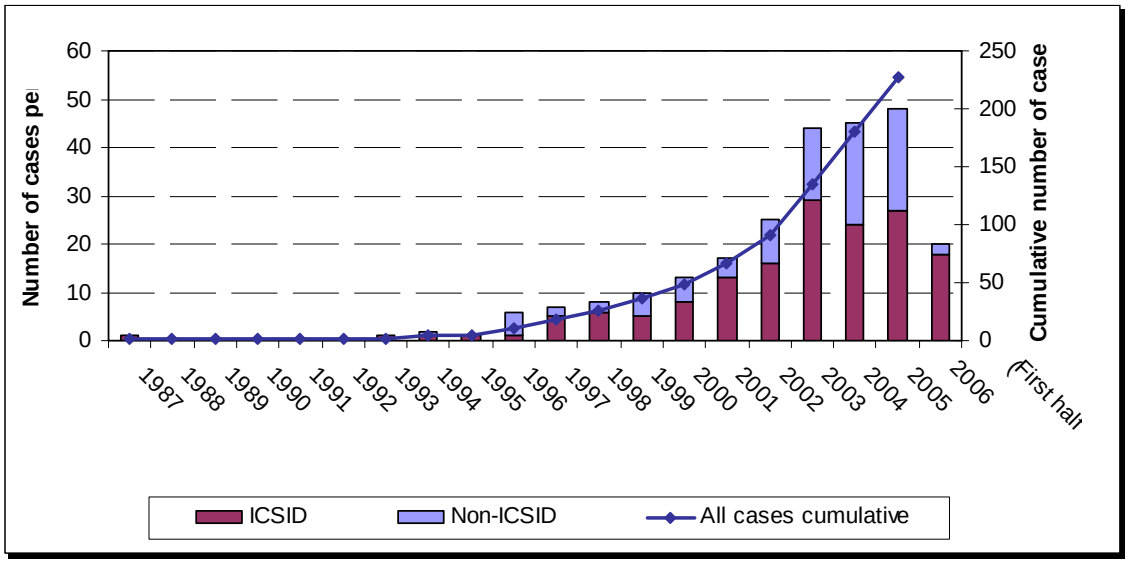
D. Investor–State disputes

29. In 2005, the number of known treaty-based investor–State dispute settlement (ISDS) cases grew by 50, and in the first half of 2006 another 20 cases were filed, bringing the total number of known treaty-based cases to a new peak of 248 by the end of June 2006 (figure 6).[4] The 2005 increase is the highest annual increase ever recorded, but the 2006 figure appears to indicate a slowdown in the recent dramatic growth of ISDS cases. Out of the total of 248 cases, 156 were filed with ICSID. Other disputes were initiated under the UNCITRAL Arbitration Rules (65), the Stockholm Chamber of Commerce (18), the International Chamber of Commerce (4), and ad hoc arbitration (4). The remaining case concerned the Cairo Regional Centre for International Commercial Arbitration. While arbitration awards in

[4] This number does not include cases where a party signalled its intention to submit a claim to arbitration but has not yet commenced the arbitration (notice of intent); if these cases are submitted to arbitration, the number of pending cases will increase.

general have helped to clarify the meaning and content of individual treaty provisions, some inconsistent decisions in recent years also created uncertainty. For example, arbitration tribunals arrived at conflicting conclusions with regard to the scope of investor–State dispute settlement procedures, the legal implications of the so-called umbrella clause, the observance of so-called cooling-off periods and the scope of the MFN clause.[5]

Figure 6. Known investment treaty arbitrations (cumulative and newly instituted cases, 1987 – end-June 2006)



Source: UNCTAD.

30. At least 61 Governments – 37 of them in the developing world, 14 in developed countries and 10 in Southeast Europe and the Commonwealth of Independent States – have faced investment treaty arbitration. Forty-two claims have been lodged against Argentina, 39 of which relate at least in part to that country's financial crisis. The number of claims against Argentina peaked in 2003 with 20 claims. Mexico has the second highest number of known claims (18), most of them falling under NAFTA and a handful under various BITs. The United States and the Czech Republic also faced a sizeable number (11 each). Canada (9) India (9), Ecuador (8), Egypt (8), the Republic of Moldova (8), Poland (7), Romania (7) and the Russian Federation (7) also figure prominently.

31. A number of important awards and decisions were rendered in 2005 and in the first half of 2006.[6] They interpret key elements of investment protection, such as the principle of fair and equitable treatment,[7] the minimum standard of treatment under international law,[8] the standard of full protection and security,[9] the scope of the MFN principle,[10] the meaning of "in

[5] See UNCTAD (2005a); Schreuer (2006) (with further reference to the pertinent awards).
[6] See also UNCTAD (forthcoming a, 2005b).
[7] *Eureko B.V. v. Poland*, Partial Award, 19 August 2005; *Noble Ventures Inc. v. Romania*, ICSID Case No. ARB/01/11, Award, 12 October 2005; and *Azurix v. The Argentine Republic*, ICSID Case No. ARB/01/12, Award 2006.
[8] *Methanex v. United States*, UNCITRAL, Final Award, 3 August 2005.
[9] *Eureko B.V. v. Poland*, Partial Award, 19 August 2005.

like circumstances" in connection with the non-discrimination principle,[11] the issue of regulatory taking,[12] the effect of the so-called umbrella clause,[13] the notion of "effective control" and the meaning of an admission clause according to which foreign investment is permitted subject to the laws of the host country.[14] Other awards rendered in 2005 dealt with the definition of "investment" and the "cooling-off" period prior to the initiation of arbitration.[15]

II. THE EVOLUTION OF BITs

32. Despite the recent increase in PTIAs, BITs remain by far the most numerous international legal instruments to promote and protect foreign investment. BITs concluded since the late 1990s continue to have a similar structure and content than earlier BITs (UNCTAD, forthcoming b). However, the fact that most BITs address basically the same issues does not mean that they have the same underlying rationale, that all agreements provide the same degree of investment protection or that they have evolved following a homogeneous pattern over the last decade. Rather, the enormous increase in BITs during the past decade has resulted in a greater variety of approaches with regard to individual aspects of their content. A small number of BITs have introduced some significant innovations. These BIT developments have also been reflected in the investment chapters of free trade agreements and other recent economic integration agreements (UNCTAD, 2006a).

A. Similarities and dissimilarities between BITs

33. Core elements found in most BITs include provisions on the scope of application, entry and establishment of investment, fair and equitable treatment, national treatment and MFN treatment, expropriation and compensation, transfer of funds and dispute settlement, both between contracting parties and between a contracting party and an investor. [16] However, despite including provisions addressing basically the same issues, BITs negotiated over the last decade have taken a variety of approaches concerning specific aspects of investment promotion and protection. Two main models can be distinguished.

34. Continuing with a trend that already existed in the mid-1990s, the overwhelming majority of BITs negotiated during the last decade follow the traditional "admission" model. These agreements apply to investment only once it has been admitted into the host country in accordance with the latter's domestic laws and regulations. Within this group of BITs,

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[10] *Plama Consortium Limited v. Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 8 February 2005; and *Telenor Mobile Communications AS v. Republic of Hungary*, ICSID Case No. ARB/04/15 Award, 13 September 2006.

[11] *Methanex v. United States*, UNCITRAL, Final Award, 3 August 2005.

[12] Ibid.

[13] *Impreglio S.p.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/3, Decision on Jurisdiction, 22 April 2005; *Eureko B.V. v. Poland*, Partial Award, 19 August 2005; *Noble Ventures Inc. v. Romania*, ICSID Case No. ARB/01/11, Award, 12 October 2005.

[14] *Aguas del Tunari v. Republic of Bolivia*, ICSID Case No. ARB/02/3, Decision on Jurisdiction, 21 October 2005.

[15] *Consorzio Groupement L.E.S.I. v. Algeria*, ICSID Case No. ARB/03/8, Award, 10 January 2005; *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakista*n, ICSID Case No. ARB/03/29, Decision on Jurisdiction, 14 November 2005.

[16] It is difficult to define in detail the typical typology of a traditional BIT. For a detailed analysis of this typology, see UNCTAD (1998).

important differences exist regarding the degree of precision of several key obligations applying to established investments. A minority of BITs afford relatively little protection to foreign investment. For instance, these BITs do not provide national treatment even after the investment has been admitted in accordance with the laws and regulations of the host country. In other BITs falling into this category, standards such as freedom of transfers or even fair and equitable treatment have been subject to domestic legislation, weakening the binding character of BIT obligations.

35. Another – relatively small – category of BIT imposes a higher degree of discipline on the contracting parties compared to the previous categories. These agreements are geared to both investment liberalization and protection. In addition to applying to investments both in the pre- and post-establishment phases, these BITs include commitments on certain issues often not covered by treaties based on the "admission" model, such as performance requirements, top managerial personnel, and, more recently, transparency. These are the BITs negotiated by the United States since the 1980s, by Canada after the mid-1990s, and by Japan at the beginning of this century. Over the last ten years, these countries have concluded more than 40 new BITs providing national treatment and MFN treatment in the pre-establishment phase. However, considering that during this period more than a thousand agreements were negotiated, these BITs are still a small minority.

36. While the overwhelming majority of BITs continue to use traditional treaty language, an emerging number of agreements include new elements (see section B below). Notwithstanding these new developments, there is a clear trend towards consolidation of the basic content of the main BIT provisions. This trend is further supported by the growing body of case law interpreting these BITs, even though arbitral awards have not always been consistent.

B. Innovations

37. As said above, while most BITs have a similar basic structure and content, there have been some key developments in the last couple of years. With the exception of the first subsequent category ("protection of public policy concerns"), all other types of innovation are mainly limited to BITs concluded by a few countries, including Canada, Colombia, Japan, the Republic of Korea and the United States.

1. Protection of public policy concerns

38. Against the background of the ongoing debate on balancing the rights and obligations of both investors and host countries, a growing number of countries emphasize in their BITs that *investment protection must not be pursued at the expense of other legitimate public concerns*. To this end, there is greater recourse to general treaty exceptions, thereby safeguarding the right of the host country to enact regulations – even ones inconsistent with the obligations in the BIT. In addition to the "traditional" areas where such exceptions have been a common feature of BITs since many years – namely taxation and regional economic integration[17] – more agreements now also exempt from the scope of the BIT – fully or partially – host country measures related to such diverse fields as essential security and public order, protection of health, safety and natural resources, cultural diversity, and prudential measures for financial services. These exceptions clarify the scale of values in the

[17] For a detailed discussion of this issue, see UNCTAD (2005c).

policymaking of contracting parties and subordinate investment protection to these other key policy objectives.

39. The proliferation of general exceptions does not follow a particular regional pattern. Rather, the increase in general treaty exceptions in BITs is a *worldwide trend* (UNCTAD forthcoming b). However, some countries emphasize the protection of certain policy objectives more than others.[18]

40. Instead of using general exceptions, other BITs have included positive language – either in their preambles or in specific provisions in the body of the text – with a view to reinforcing the commitments of the contracting parties to safeguard certain values, basically the protection of health, safety, the environment, and the promotion of internationally recognized labour rights. Although this technique has legal effects different from those of a general exception, it sends the same political signal that contracting parties do not place investment protection above other important public policy objectives. Once again, this approach is *not limited to specific countries or regions* (UNCTAD forthcoming b).

2. Other innovations

41. A small group of BITs include further innovations in investment rulemaking. The new model BITs of Canada and the United States exemplify this approach. The normative evolution has focused on several areas: clarifying individual BIT provisions; providing greater transparency; and improving the transparency and predictability of dispute settlement.

42. *(i) Clarification of individual BIT provisions*: While most BITs continue to use very general language in their provisions on fair and equitable treatment and expropriation, recent BITs of Canada and the United States have deviated from this approach and spell out in more detail the content of some core provisions. One example is the revision of the wording of various substantive treaty obligations. The new Canadian and United States model BITs, responding to the technical intricacies faced in the implementation of the investment chapter of NAFTA and to the numerous investor–State disputes to which the two countries have been a party, use more detailed language and elaborate on the meaning of absolute standards of protection, in particular, the minimum standard of treatment in accordance with international law and indirect expropriation. In addition, both BIT models include annexes specifying guidelines and criteria in order to determine on a case-by-case basis whether indirect expropriation has in fact taken place.

43. *(ii) Transparency*: Recent BITs of Canada and the United States have dealt explicitly with the issue of transparency. The rationale and content of the obligations on this subject have been gradually evolving. In addition to a trend towards conceiving transparency as an obligation to exchange information between contracting parties, this kind of BITs views transparency as a reciprocal commitment between the host country and the investor. Furthermore, transparency is extended to the process of domestic rulemaking, aimed at allowing investors and other interested persons to participate in it.[19]

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[18] For example, the use of the exception for the protection of cultural diversity is practically limited to BITs negotiated by Canada and France.

[19] These transparency obligations are not subject to the ISDS provisions – that is, they are not enforceable by investors.

44. *(iii) Investor–State dispute settlement*: Another feature of recent Canadian and United States BITs is their significant innovation regarding investor-State dispute settlement. This includes greater and substantial transparency in arbitral proceedings, open hearings, publication of related legal documents, and the possibility for representatives of civil society to submit *amicus curiae* briefs to arbitral tribunals. Other new detailed clauses provide for a more law-oriented, predictable and orderly conduct at the different stages of the investor–State dispute settlement process.[20] The BIT between the United States and Uruguay (2005) not only provides for a special procedure at the early stages of the investor–State dispute settlement process aimed at discarding frivolous claims, but also envisages the possibility of setting up an appellate mechanism to foster a more consistent and rigorous application of international law in arbitral awards.

III. IMPLICATIONS AND CHALLENGES

45. The enormous increase in BITs has resulted in a remarkable degree of conformity as far as their *basic structure and content* is concerned. Apart from the traditional divide between BITs with and without liberalization commitments, there is no major disagreement about what should be the core elements of a BIT and what basic content its key provisions should have. On the other hand, despite this broad general consensus, the picture becomes much more diverse when one looks into the details of individual BIT provisions. In this respect, it is fair to say that the level of variation between BITs has increased in recent years. While some differences relate to the substance of the provisions, others concern only minor linguistic diversities – albeit sometimes with major implications.

46. A few issues stand out as major new developments. They include the introduction of additional elements of investment protection, greater emphasis on key public policy concerns as a counterweight to investment protection, clarification of individual treaty provisions, greater transparency and more detailed rules on investor–State dispute settlement.

47. The consolidation of core BIT provisions should contribute to facilitating future international investment rulemaking and gives foreign investors more assurance of what they can reasonably expect from host countries in terms of investment protection. The greater diversity of BITs when it comes to the details of the agreement reflects the flexibility that countries would like to have in choosing the partners to enter into an agreement and to tailor individual agreements to their specific situations, development objectives and public concerns. Furthermore, more elaborate rules may enhance legal clarity on rights and obligations and fill existing gaps in the overall treatment of foreign investment.

48. On the other hand, developments in BIT negotiations also mean that a new pattern in international investment rulemaking is emerging. In addition to the different approaches to investment liberalization in BITs, agreements can now also be distinguished according to their degree of complexity. However, it should be noted that BITs with such more elaborate structures are still a relatively small minority. Furthermore, to some extent these BITs might *look* more different on paper than they really are, since they are not meant to substantially deviate from or even contradict "traditional" BITs. Rather, to some degree these more complex BITs "only" spell out explicitly what contracting parties to conventional agreements implicitly have in mind when concluding the treaty. All this suggests that these differences

[20] The Canadian model BIT, for example, even includes specific standard waiver forms to facilitate waivers as required by the agreement for purposes of filing a claim.

are less significant than the divide between BITs that include liberalization commitments and those that do not.

49. Nevertheless, the growing diversity of BITs and other IIAs poses new challenges in terms of coherence. The risk of incoherence is especially great for developing countries that lack expertise and bargaining power in investment rulemaking and that may have to conduct negotiations on the basis of divergent model agreements of their negotiating partners (UNCTAD, 2006b). Already in the past, developing countries concluded different kinds of BITs, depending on whether their developed market economy treaty partner excluded or included pre-establishment obligations. With the recent emergence of more complex BITs, an additional layer of potential incoherence has been introduced.

50. One example is the more frequent recourse to exception clauses in recent BITs. It could mean that a developing country's measures to protect certain public values (e.g. national security or the environment) are not subject to the discipline of some BITs while other BITs (or other IIAs) cover them. Another illustration is the interpretation of the international minimum standard in accordance with the principles of customary international law in recent Canadian and United States BITs. Although these interpretative clauses are only meant to clarify the content of the provision and do not therefore intend to introduce substantive amendments, they may nevertheless have a decisive impact on arbitration proceedings. As a result, tribunals might arrive at different conclusions with regard to the legality of basically the same host country measure, depending on whether the BIT contains an interpretative statement or not.

51. It remains to be seen whether the future development of BITs will result in the gradual convergence of the different models. To a considerable extent, this will depend on the further evolution of investment disputes. Many of the recent changes that Canada and the United States introduced into their BITs reflect their arbitration experience. If ever more countries become defendants in investment disputes and if they consider that arbitration tribunals have too much discretion in interpreting BIT provisions, they might wish to follow the Canadian and United States approach. However, it is also possible that the substantial increase in arbitral awards will result in a consolidation of case law that makes the outcome of future arbitration both more predictable and acceptable, thereby reducing the need for interpretative statements in BITs (UNCTAD, forthcoming a).

52. For the time being, the MFN principle included in most BITs might contribute to furthering coherence between different agreements. It might ensure, at least in principle, that an investment from a country with a "lower" protection standard BIT will receive treatment no less favourable than the treatment granted to an investment from a country with a "higher" protection standard BIT. The MFN standard might therefore have the effect of “levelling the playing field” between the protection that is provided to investors of different nationality.

53. Applying the MFN principle to BITs with different degrees of complexity can be a challenging task. On the one hand, it might mean that the BIT provision with the higher level of sophistication becomes applicable. This could be the case, for instance, if one BIT grants foreign investors additional rights with regard to transparency or in dispute settlement proceedings. On the other hand, the greater complexity of one BIT might also imply a reduction in the level of investment protection as compared with other BITs, as a result of

which this BIT provision could become inapplicable.[21] Such policy coherence through the MFN clause could render useless the efforts of contracting parties to distinguish their BIT from other agreements. The point should also be made that the scope and effect of the MFN clause have become uncertain in the light of some recent contradictory awards.[22]

54. Another challenge for developing countries in future BIT negotiations has to do with the fact that a growing number of them are becoming capital exporters. As a result, they are not only concerned about ensuring sufficient flexibility for themselves in regulating inward FDI. They also seek to provide their investors with ample protection abroad. Reconciling these two potentially conflicting interests may not be easy.

55. Yet another challenge arises out of the emerging wave of new policy measures targeting FDI in some countries, including the renationalization of domestic industries and the re-emergence of national security and sovereignty concerns. This poses the question of how these new developments might impact on future BITs in particular and on IIA rulemaking in general. While there might be calls for a reinforcement of treaty provisions, there might also be greater reluctance to enter into obligations that limit countries' sovereignty over natural resources or affect other sectors of strategic importance.

IV. THE WAY FORWARD

56. International investment rulemaking poses particular challenges for developing countries. One consequence of this situation is the growing need for policy research and analysis, as well as capacity-building, to help developing countries in assessing the implications of different policy options before entering into new agreements, identifying the potential obligations deriving therefrom and implementing commitments made. Rigorous policy analysis of the evolution of the IIA universe that addresses the challenges arising out of its systemic inconsistencies and further international consensus-building on key development-related issues are other vital tasks. This includes more research on emerging trends concerning internationally recognized principles in investment rulemaking and the identification of common elements.

57. This matter could be further pursued through the creation of an UNCTAD Standing Expert Group on International Investment Agreements and Development that focuses on systemic issues in the area of international investment rule-setting. Among its tasks could be (i) to monitor and examine the rapidly growing IIA universe, including the evolving jurisprudence from investment disputes; (ii) to identify major similarities and dissimilarities in IIAs; (iii) to analyse the implications of the system-immanent problems of the IIA patchwork, including its systemic inconsistencies; (iv) to pay particular attention to the development dimension of these problems; and (v) to facilitate multilateral cooperation in international investment policy setting. This could be pursuant to the decision of the tenth session of the Commission, which states inter alia that "UNCTAD should serve as *the key focal point* in the United Nations system for dealing with matters related to international investment agreements, and continue to provide *the forum* to advance the understanding of issues related to international investment agreements and their development dimension […]."

[21] For example, if BIT A includes an unqualified obligation to grant fair and equitable treatment and BIT B states that such treatment refers only to the international minimum standard, the MFN clause in BIT B might override this statement. The result might be similar if one BIT includes a specific exception and the other does not.
[22] See UNCTAD (forthcoming a, 2005d).

(emphasis added).[23] Furthermore, the UNCTAD Panel of Eminent Persons and the Mid-Term Review have called for the establishment of Standing Expert Groups.[24]

58. Such a Standing Expert Group could facilitate an exchange of experiences and views on these issues and work towards formulating international policy instruments to accompany investment rulemaking at the bilateral, subregional, regional and interregional levels. In the longer run, it might contribute to a possible future discussion on multilateral approaches to the international system of investment and its development dimension, as was reflected in the recommendations of the reports of the UNCTAD Panel of Eminent Persons and the World Commission on the Social Dimension of Globalization.[25]

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[23] See TD/B/COM.2/71 of 24 March 2006, paragraph 8.

[24] See UNCTAD Panel of Eminent Persons (2006), paragraph 62 and recommendation No. 14; and UNCTAD (2006c, paragraph 32(h)).

[25] See ILO 2004.

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